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SUBJECT: JAPANESE MORNING PRESS HIGHLIGHTS 12/21/06

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(1) Optimism over budget looks a bit premature

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3) Prime Minister's Official Residence (Kantei)

Prime Minister's schedule, December 20

NIHON KEIZAI (Page 2) (Full)
December 21, 1996

09:03

Attended at Kantei emergency cabinet meeting. Internal Affairs Minister Suga remained in the room. Met later with Vice Finance Minister Fujii and Budget Bureau chief Tsuda, followed by Economic and Fiscal Policy Minister Ota, Special Advisor Nemoto and Assistant Deputy Chief Cabinet Secretary Saka.

10:03

Attended a meeting to strengthen functions of Kantei regarding national security.

11:38

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Met Special Advisor Yamatani and others.

12:47

Met Expo 2005 Aichi Chairman Shoichiro Toyoda.

13:33

Held talks with LDP Secretary General Nakagawa for New Year's project by Chugoku Newspaper at LDP headquarters.

14:59

Met at Kantei with Japan-US Economic Cooperation Council Chairman Junichi Ujiie. Met Japan WBC manager Sadaharu Oh and other WBC members, joined by former Prime Minister Mori. Mori remained in the room.

16:15

Met with Acting Secretary General Ishihara and Lower House members Yasutoshi Nishimura and Yoichi Miyazawa. Attended meeting of the Economic and Fiscal Policy Council.

17:36

Met with Foreign Minister Aso.

18:43

Returned to his official residence.

4) Tax Commission Chairman Honma to resign over lodging scandal, blow to Abe government

ASAHI (Top Play) (Full)
December 21, 2006

The government's Tax Commission Chairman Masaaki Honma, a professor at Osaka University, yesterday firmed up his intention to resign his post, according to government officials. He appears to have determined that it would be difficult for him to devote himself to his duty since there are increasing calls for him to voluntarily step down from his post over the fact that he had lived without authorization at a government-paid apartment in a prime location in Tokyo. Prime Minister Shinzo Abe appointed him as chairman of the commission in an attempt to demonstrate a policy of placing priority on economic growth led by the Prime Minister's Official Residence (Kantei). If Honma resigns after serving in his post only one and a half months, Abe's responsibility for appointing him will be called into question. As a result, Honma's resignation will inevitably weaken the cohesion of the Abe administration, over which dark clouds are already appearing due to the reinstatement of postal rebels into the Liberal Democratic Party (LDP) and other matters.

Abe has repeatedly said he has no intention to replace him, noting, "I want him to fulfill his duty." A government official, however, indicated yesterday that the prime minister would eventually agree to his resignation, saying, "There is no change in the prime minister's position, but we cannot prevent him from stepping down."

Honma was named chairman of the Tax Commission on Nov. 7, expecting to serve in the post for three years. Rejecting the reappointment of Hiromitsu Ishi as chairman of the panel whom the Finance Ministry recommended, the Kantei picked Honma, who advocates a corporate tax

cut, making clear the policy of prioritizing economic growth. The Tax Commission on Dec. 1 submitted to the government a report on tax reform for fiscal 2007 recommending a study of the corporate tax rates, including a review of the depreciation system and other aspects of corporate taxes.

However, a weekly magazine on sale on Dec. 11 carried an article that Honma allegedly lived with a woman other than his wife in a government-paid condominium. After that, many LDP members criticized

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him, noting that what he did was inappropriate for a person who asks the public to agree to pay more tax.

At a press conference on Dec. 13, Honma denied the allegation that he was living with a woman other than his wife but revealed that he moved out of the government-sponsored apartment.

The rent for the 3LDK government-paid apartment in Shibuya Ward is about 77,000 yen per month. Honma as chairman of an expert panel of the Economic and Fiscal Policy Council compiled in September a report calling for promotion of selling national assets, including holdings for public servants. Amid growing calls for Honma's dismissal, only Prime Minister Abe and Chief Cabinet Secretary Shiozaki were supporting Honma.

5) Government's tax panel chair Honma's resignation to deal blow to government, as he is "symbol of reform"

ASAHI (Page 2) (Excerpts)
December 21, 2006

The tide of opinion in the government and ruling parties about Government Tax Commission Chairman Honma's course of action is that his resignation will be unavoidable. If the scandal dragged on into the ordinary Diet session to be convened early next year, "It could put the government at risk," given that the scandal would be made an easy target for attacks in tax system reform negotiations that envision a possible hike in the consumption tax after the Upper House election, a high-level government official said. Meanwhile, a stumble in Prime Minister Abe's selection of personnel could cast a blight on his reform line.

Late yesterday, when asked by reporters about Honma's course of action, Abe stated, "He has deep insight into the tax system. I hope he will devote himself to his duties and regain public confidence." Abe thus stressed he did not waver.

But, a report of recommendations released by the Government Tax Commission led by Honma was exposed to such criticism as "giving favorable treatment to companies but a veiled possible hike in the consumption tax," not getting along with the ruling Liberal Democratic Party's (LDP) tax panel's policy. The moment the scandal of Honma's allegedly inappropriate use of a public residence was reported, calls for his resignation from the post erupted among senior LDP tax panel members. Even cabinet members made cold remarks about Honma one after another.

The government and ruling parties feared that a scandal involving the person responsible for the tax system reform could fuel criticism of the government in tax system reform negotiations ahead of the Upper House election. It is also expected that the opposition camp will strike at this scandal in the course of tax system reform debate in the ordinary Diet session. The government and ruling camp were highly concerned about the possibility that "once a scandal is reported, it will be rehashed over and over again," as a high-level government official put it.

On the other hand, Honma was an aggressive private-sector member of the Council on Economic and Fiscal Policy (CEFP) and was seen as the symbol of continuing the reform line. Criticisms of Honma heard in the ruling camp in part entailed objections to Abe's attitude of continuing the reform line. Abe, unlike former Prime Minister

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Koizumi, who remained protective of his appointed cabinet members and LDP executives despite calls for their resignations, may give the impression that he has given in to the ruling parties' calls.

6) SDP chief criticizes Minshuto's way of dealing with Diet session; PNP, JCP chairman also unhappy

MAINICHI (Page 5) (Full)
December 21, 2006

Social Democratic Party (SDP) head Mizuho Fukushima during a press conference yesterday criticized the Democratic Party of Japan's (DPJ or Minshuto) approach to the Diet session. She rapped the party for refusing to submit a motion censuring Prime Minister Shinzo Abe in the final stage of the Extraordinary Diet session, noting, "It was rotten and regrettable. We are annoyed." She played up a stance of attaching importance to maintaining an independent posture instead of aiming for a united front by opposition parties. She stated, "We areQ#3N\$U~y[omQ the same day stated, "I want to demand an overall replacement of senior Minshuto Diet Policy officials." Japanese Communist Party (JCP) Chairman Kazuo Shii also stated during a press conference on Dec. 19: "Minshuto has come up with a policy of confronting the opposition camp under the leadership of party head Ichiro Ozawa. However, the details are missing." Dissatisfaction with Minshuto is growing among opposition parties.

7) DPJ rushing to field candidates for Upper House election next summer in single-seat constituencies

MAINICHI (Page 5) (Excerpts)
December 21, 2006

In a bid to catch up with its late start, the Democratic Party of Japan (DPJ or Minshuto) is rushing to field candidates in single-seat constituencies, which are said to hold the key to the outcome of the Upper House election next summer. Party head Ozawa visited Nagasaki twice last week. This week he visited Okayama, Shiga and Fukui. He has so far visited only single-seat districts. The party has now fielded candidates in 15 single-seat districts out of 29, picking three this month. It will likely be able to field candidates, including those endorsed jointly with other opposition parties, in 20 districts, approaching the LDP's 23.

Strategy to encroach upon LDP's territories

Ozawa on Dec. 20 held a press conference in Otsu City, Shiga Prefecture, where the DPJ approved a candidate on the previous day. Commenting on the situation of fielding candidates for single-seat districts, he stressed, "We are smoothly picking candidates. We could be fully ready for aiming for a majority seats of more than 15."

8) LDP's Takebe launches new group "New Breeze" with 24 young lawmakers

YOMIURI (Page 4) (Full)
December 21, 2006

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Tsutomu Takebe, former secretary general of the ruling Liberal

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Democratic Party (LDP), yesterday launched a new group called "New Breeze (Atarashii Kaze)" which he heads.

A total of 24 lawmakers, including Takebe, attended yesterday's inaugural party held in a Tokyo hotel. The group consists of mainly junior LDP members who are unaffiliated with any faction and are serving their first or second term in the Diet. Takebe said in the party:

"Former Prime Minister Koizumi's statement that there would be no growth without reforms is not a slogan for just one government but

is Japan's new guidepost. I want to do my best to push forward with the reform program."

House of Representatives member Yukari Iijima (proportional representation Hokkaido) proposed that the group make efforts to revitalize the city of Yubari in Hokkaido, which is suffering from financial difficulties and whose population is on the decrease. The group decided on a policy line of working on measures to revitalize the city, after carrying out on-the-spot research.

9) JDA, MOF agree on allocation of US force realignment costs under separate budget framework

YOMIURI (Page 2) (Full)
December 21, 2006

In the tug-of-war between the Defense Agency (JDA) and Ministry of Finance (MOF) over how to treat expenditures to finance US force realignment programs, a settlement was reached in effect yesterday as the Finance Ministry earmarked 7.24 billion yen as realignment costs under a separate budget framework from the FY2007 defense budget in its draft budget unofficially announced the same day. Members in the Liberal Democratic Party, which was calling for setting up a separate framework, welcomed the MOF decision, with former Defense Agency Director General Gen Nakatani remarking: "It is significant that approval was given to a separate budget framework for the initial year of the programs. This decision is likely to affect budget compilation next fiscal year and beyond."

In the defense budget, there is no classification of "separate framework." But outlays related to SACO (Special Action Committee on Okinawa) aimed to reduce the burden on the local communities housing US military bases are separated from expenditures to finance usual defense matters, such as costs for front-line equipment and personnel. This measure has been conventionally taken in response to such a political request as that. "It is undesirable to hinder Self-Defense Force's activities as a result of the defense budget being trimmed in order to lighten the burden on local communities in Okinawa," said an LDP member responsible for national defense policy.

JDA and MOF agreed yesterday to allocate spending on measures to reduce the burden on the local communities to be affected from the relocation of the US Marine Corps' Futenma Air Station in Okinawa and other plans under a separate slot, like the case of SACO-linked outlays.

Next year, the mid-term defense buildup plan (FY2005 - FY2009) is due to be reviewed. In the spar over a separate budget framework

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between JDA and MOF, the JDA's request was accepted this year. But such a tactful game is likely to heat up again next year. One Defense Agency official said, "The crucial stage will come three or four years from now, when US force realignment costs is will balloon to an annual 100 to 200 billion yen."

10) Finance Ministry proposes 5.05 billion yen in US force realignment-related subsidies; Affected municipalities to be classified into four levels

MAINICHI (Page 3) (Full)
December 21, 2006

The Finance Ministry's draft budget for fiscal 2007 includes 5.05 billion yen in subsidies to municipalities that would bear greater burdens as a result of the realignment of US forces in Japan. The system is designed to increase subsidies in four stages according to their level of acceptance of burdens. The draft budget also includes 10 billion yen that is part of a continuing economic package for the northern part of Okinawa. The carrot-and-stick approach to curry favor with affected municipalities might draw protests from local residents.

In a joint government and ruling coalition meeting on Dec. 15, Defense Agency Director-General Fumio Kyuma expressed his eagerness

for progress in US force realignment, saying: "To meet the expectations of municipalities that have already accepted US force realignment, we are going to seek cooperation of municipalities that have yet to accept it."

Realignment subsidies will become a pillar in 10-year US force realignment promotion legislation to be submitted to the Diet in the next regular session. Subsidies are expected to total 100 billion yen over 10 years.

The envisioned system is similar to the special defense facilities subsidies system covering municipalities with airports, training ranges, and the like. The new system is unique in that the range has expanded to cover "soft" projects, such as lecture meetings, in addition to public works projects.

The Defense Agency plans to increase subsidies depending on municipalities' responses based on four levels: (1) local heads' announcement of acceptance of US facilities, (2) implementation of environmental assessments, (3) start of construction, and (4) relocation of troops. The program is aimed at applying mental pressure on local governments that have yet to agree to accept US military facilities, such as Okinawa, by discriminating them against others depending on the degree of their cooperation.

11) MD-related budget adds up to 182.6 billion yen

ASAHI (Page 4) (Full)
December 21, 2006

The Finance Ministry's fiscal 2007 budget plan incorporated a budgetary estimate of 182.6 billion yen for spending related to missile defense, marking an increase of 30 percent over the current fiscal year in response to North Korea's missile launches and nuclear test. Japan is currently working together with the United States to develop a missile defense system, for which the Finance Ministry has approved a seven-fold outlay of 21.6 billion yen.

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The Finance Ministry's draft budget approves spending to co-develop the Standard Missile 3 (SM-3), a sea-based missile defense system, with the United States, incorporating an increase of 18.6 billion yen from 3.0 billion yen budgeted for the current fiscal year. The SM-3 development project, currently at the stage of design, will now go on to the stage of making a prototype. In addition, the supplementary budget for the current fiscal year incorporated an additional outlay of 7.6 billion yen to move up Japan's purchase of Patriot Advanced Capability 3 (PAC-3) ground-based missiles from a US manufacturer.

Japan is going to step up its missile surveillance and warning readiness, and the Finance Ministry has approved a total of 7.0 billion yen in the extra budget for the current fiscal year and in the draft budget for next fiscal year to renovate electronic intelligence aircraft detecting missile launch signs. Japan will share detected intelligence with the United States.

12) Appropriation of 7.6 billion yen for purchases of PAC3 missiles in supplementary budget ahead of schedule

MAINICHI (Page 5) (Full)
December 21, 2006

The government earmarked approximately 7.6 billion yen for early purchases of Patriot Advanced Capability-3 (PAC-3) surface-to-air missiles in the fiscal 2006 supplementary budget, adopted at a cabinet meeting on Dec. 20. Though it had originally set that amount aside in a budget appropriation request for fiscal 2007, following the test-launches of missiles by North Korea, it has frontloaded the appropriation together with approximately 4.5 billion yen for expenses to repair EP-3 electronic intelligence gathering planes. Approximately 8.4 billion yen was also earmarked as research expenses for the transfer of Futenma Air Station to the coastal part of Camp Schwab in Nago City, Okinawa. In the fiscal 2006 supplementary budget 71.1 billion yen, the largest amount to date,

was appropriated for defense-related expenses.

13) Futenma relocation: 10 billion yen earmarked for Okinawa's northern economic development

ASAHI (Page 4) (Full)
December 21, 2006

In connection with the issue of relocating the US Marine Corps' Futenma Air Station in Ginowan City, Okinawa Prefecture, to the island prefecture's northern coastal city of Nago, the Finance Ministry has earmarked a budgetary estimate of 10 billion yen in its fiscal 2007 budget plan for a package of economic development measures for Okinawa's northern districts hosting an alternative facility for Futenma airfield.

Japan and the United States have agreed to realign US forces in Japan. Meanwhile, the government made a cabinet decision in May to discontinue the northern development package. However, the government, in order to facilitate talks with base-hosting localities, decided to continue the package at the request of Okinawa Gov. Hirokazu Nakaima, who was elected for the first time with his acceptance of Futenma relocation within the prefecture.

14) ODA budget now 40 percent below peak period, marking eighth

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consecutive yearly drop

NIHON KEIZAI (Page 5) (Full)
December 21, 2006

Under the Finance Ministry's draft budget for FY2007, the government will reduce outlays for official development assistance (ODA) projects by 4 percent below the initial budget for the current fiscal year to 729.3 billion yen. This figure is about 40 percent less than the 1,168.7 billion yen recorded in FY1997.

In the draft supplementary budget for FY2006, 86.2 billion yen was earmarked as ODA funds to finance reconstruction and development projects in Iraq. Although the ODA budget will be cut by 4 percent in the Finance Ministry's draft budget, a ministry official said, "The ODA budget will increase in effect if the outlays in the supplementary budget are added. We gave consideration to increasing ODA projects."

Former Prime Minister Junichiro Koizumi promised in 2003 to augment 10 billion dollars in ODA projects. With the record in 2004 as the standard, about 80 percent of Koizumi's pledge is likely to be attained by 2006. However, China's repayments of yen loans have speeded up, so ODA projects may not increase as expected. An official of the Foreign Ministry voiced concern, "It might become difficult to attain the target."

Regarding the Foreign Ministry's request for increases in personnel and diplomatic establishments abroad as part of efforts to strengthen the nation's diplomatic capabilities, outlays were not allocated, and the request will be discussed in restoration negotiations.

The fixed number of Foreign Ministry personnel is expected to increase by 32 in the end. If those farmed out from other government agencies are included, the net increase is projected to be 51.

15) Abduction-related budget up 10-fold to 473 million yen

ASAHI (Page 4) (Abridged)
December 21, 2006

The Finance Ministry yesterday posted its draft budget in its budget compilation for fiscal 2007. The posted budget plan incorporates an estimate of 473 million yen for a government taskforce, headed by Prime Minister Abe, to send and collect information about abductees. The Finance Ministry has approved almost all abduction-related budget requests to the full, and the approved amount of these budget requests is nearly 10 times larger than 51 million yen budgeted for

the current fiscal year. The supplementary budget for the current fiscal year has also earmarked 226 million yen for abduction-related appropriations.

The draft budget endorses 134 million yen for broadcasting to North Korea and 81 million yen for stepping up the government's preparedness to collect information about abductees.

16) 6-party talks: Japan seeking approval for mention of "abduction" in document

NIHON KEIZAI (Page 2) (Excerpts)
December 21, 2006

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Kei Sekiguchi, Beijing

The Japanese government intends to appeal to other member nations of the six-party talks on the need to mention the importance of resolving the issue of Japanese citizens abducted by North Korea in a document that will summarize the results of the ongoing six-party talks. The key to whether this will be realized is whether Japan can make other members understand its position of attaching equal importance to the abduction issue as the nuclear issue. North Korea, which has stated (that the abduction issue) was already settled, is certain to oppose Japan.

The top US negotiator at the six-party talks, Assistant Secretary of State Christopher Hill has proposed documenting the results of the six-party talks. Chief Cabinet Secretary Yasuhisa Shiozaki told a press briefing yesterday: "Japan has reiterated the need to resolve the abduction issue. If a document (about the six-party talks) is created, Japan will naturally assert (the abduction issue) be mentioned in it."

The Japanese representative to the six-party negotiations, Foreign Ministry Asian and Oceanian Affairs Bureau Director-General Kenichiro Sasae yesterday met separately with Hill and his South Korean counterpart, Chun Young Woo, director of the Office of Diplomatic Policy of South Korea's Ministry of Foreign Affairs and Trade, and confirmed close coordination among Japan, the US, and South Korea.

17) 3 Aegis ships readied for missile defense

SANKEI (Page 5) (Full)
December 21, 2006

The US Navy has completed the renovation work of mounting the Standard Missile 3 (SM-3), a sea-based intercept missile system for missile defense, on two Yokosuka-based Aegis destroyers, the USS Stetham and the USS Curtis Wilbur, a senior official of the Defense Agency said yesterday. The United States has told Japan that the two ships could go operational before Christmas. The US military has now three Aegis ships for missile defense deployed in Japan.

18) Ishiba advocates collective security

SANKEI (Page 5) (Full)
December 21, 2006

Former Defense Agency Director General Shigeru Ishiba yesterday came up with an outline of his plan for a security law in a meeting of the ruling Liberal Democratic Party's defense policy subcommittee he chairs. The government has been taking the position that Japan is constitutionally prohibited from participating in collective self-defense. The proposed law, however, allows Japan to exercise its right to collective self-defense only if a foreign country closely related with Japan comes under attack from a foreign country's armed forces. Specifically, the planned law makes it possible for Japan to participate in collective security if and when there is an armed attack against another country and if that can be regarded as an attack against Japan.

19) Sakhalin-2 project to be settled possibly today; Japanese and

European firms to sell most of their stakes to Gazprom

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MAINICHI (Page 1) (Full)
December 21, 2006

Negotiations between Japanese and European firms and a Russian firm over the management agency of the Sakhalin-2 oil and gas projects off Sakhalin, Russia, are expected to be finalized possibly today. Royal Dutch/Shell, Mitsui & Co., and Mitsubishi Corp. will sell a majority of their shares of Sakhalin Energy Investment Co., the project implementing body, to the Russian state-run gas company Gazprom. The shares will be transferred at 4-6 billion dollars (or 470-700 billion yen).

Shell made a 55 percent investment in Sakhalin Energy, followed by Mitsui's 25 percent and Mitsubishi's 20 percent. Shell will sell some 30 percent of its stake to Gazprom instead of exchanging other rights, and Mitsui and Mitsubishi will follow, with the sale of some 10 PERCENT of their respective stakes. Mitsui & Co. President Utsuda and Mitsubishi President Kojima already arrived in Russia. After the final phase of negotiations with Gazprom starting today, they will aim to reach agreement by Dec. 24.

The Russian government since this summer has hinted at suspending the project or making a claim for compensation. This move was seen as a means to let Gazprom join the project under favorable conditions. Most Japanese electricity and gas companies have signed a long contract to purchase LNG from Sakhalin-2 in 2008 or after. The Russian side has confirmed that it will respect the existing contract, but this development will likely create a source of concern for Japan's energy policy.

DONOVAN